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1 ARIZONA WATER COMPANY  
2 Robert W. Geake (No. 009695)  
3 Vice President and General Counsel  
4 3805 Black Canyon Highway  
5 Phoenix, Arizona 85015-5351  
6 Telephone: (602) 240-6860

7 Attorney for Arizona Water Company

8 **BEFORE THE ARIZONA CORPORATION COMMISSION**

9  
10 IN THE MATTER OF THE APPLICATION  
11 OF AJO IMPROVEMENT COMPANY FOR  
12 A RATE INCREASE

**DOCKET NO. WS-01025A-03-0350**

**NOTICE OF FILING  
DIRECT TESTIMONY  
AND EXHIBITS**

13 Intervenor Arizona Water Company, hereby files the Direct Testimony and Exhibits of  
14 Sheryl L. Hubbard in the above-captioned docket.

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Arizona Corporation Commission  
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DATED this 6th day of February, 2004.

ARIZONA WATER COMPANY

By: Robert W. Geake  
Robert W. Geake  
Vice President and General Counsel  
Arizona Water Company  
P.O. Box 29006  
Phoenix, AZ 85038-9006

An original and 13 copies of the foregoing, and attached documents were delivered this 6th day of February, 2004, to:

Docketing Supervisor  
Docket Control  
Arizona Corporation Commission  
1200 West Washington  
Phoenix, AZ 85007

A copy of the foregoing was Delivered/mailed this 6th day of February, 2004, to:

Jane L. Rodda, Administrative Law Judge  
Hearing Division  
Arizona Corporation Commission  
1200 West Washington  
Phoenix, AZ 85007

Fred Menzer  
Ajo Improvement Company  
New Cornelia Branch  
PO Drawer  
Ajo, AZ 85321

Michael Patten  
Roshka Heyman & DeWulf, PLC  
One Arizona Center  
400 East Van Buren Street, Suite 800  
Phoenix, AZ 85004

1 Dan Neidlinger  
2 Neidlinger & Associates  
3 3020 North 17<sup>th</sup> Drive  
4 Phoenix, AZ 85015

5 Christopher Kempley, Chief Counsel  
6 Legal Division  
7 1200 W. Washington Street  
8 Phoenix, AZ 85007

9 Mr. Ernest G. Johnson, Director  
10 Utilities Division  
11 Arizona Corporation Commission  
12 1200 West Washington  
13 Phoenix, AZ 85007

14 By: Robert W. Geale  
15 1208295.1

1 ARIZONA WATER COMPANY  
Robert W. Geake (No. 009695)  
2 Vice President and General Counsel  
3805 N. Black Canyon Highway  
3 Phoenix, Arizona 85015-5351  
Telephone: (602) 240-6860

4 Attorney for Arizona Water Company  
5  
6  
7

8 **BEFORE THE ARIZONA CORPORATION COMMISSION**

9  
10 IN THE MATTER OF THE  
APPLICATION OF AJO  
11 IMPROVEMENT COMPANY FOR  
RATE ADJUSTMENTS IN ITS WATER  
AND WASTEWATER RATES.  
12

Docket No. WS-01025A-03-0350

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18 **DIRECT TESTIMONY**  
19 **OF**  
20 **SHERYL L. HUBBARD**  
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1 I. INTRODUCTION AND QUALIFICATIONS

2 Q. What is your name, employer and occupation?

3 A. My name is Sheryl L. Hubbard. I am employed by Arizona  
4 Water Company ("Arizona Water") as Manager of Rates and  
5 Regulatory Accounting.

6 Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL  
7 BACKGROUND.

8 A. I graduated from Michigan State University with a  
9 Bachelor of Arts degree in Accounting and I am a certified  
10 public accountant. I have twenty-five years of experience  
11 with public utility accounting and regulation having been an  
12 auditor/audit manager with the Michigan Public Service  
13 Commission for seventeen of those years. During my  
14 employment with the Michigan Commission, my responsibilities  
15 included preparation of revenue requirement calculations for  
16 water, steam and electric utilities. Following my  
17 employment with the Michigan Public Service Commission, I  
18 was employed by the Arizona Corporation Commission ("ACC")  
19 as the Chief of Accounting and Rates where my  
20 responsibilities included applying statutes, rules and  
21 regulations, and ACC policies in regulating public utilities  
22 in Arizona.

23 Subsequent to my employment with the ACC, I joined  
24 Citizens Communications Company ("Citizens") as a Regulatory  
25 Accounting Manager in its Arizona Gas division. My  
26 responsibilities, with Citizens, included assuring

1 compliance with applicable state statutes and regulatory  
2 rules and decisions as well as preparation of rate cases and  
3 other regulatory filings with state regulatory agencies in  
4 Arizona and Colorado. Subsequent to my employment with  
5 Citizens Communications Company, I joined Arizona Water in  
6 my current position as Manager of Rates and Regulatory  
7 Accounting.

8 **II. PURPOSE AND EXTENT OF TESTIMONY**

9 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?**

10 A. The purpose of my testimony in this proceeding is to: 1)  
11 clarify the type of service that Arizona Water receives from  
12 Ajo Improvement Company ("Ajo Improvement"), 2) establish  
13 that the cost to serve Arizona Water is less than Ajo  
14 Improvement's other General Service customers, and 3)  
15 present Arizona Water's proposed rate design for a wholesale  
16 4-inch meter classification for Ajo Improvement under which  
17 Arizona Water would be served.

18 **III. CHARACTERISTICS OF SERVICE TO ARIZONA WATER**

19 **Q. PLEASE DESCRIBE THE CHARACTERISTICS OF THE WHOLESALE SERVICE**  
20 **ARRANGEMENT THAT EXISTS BETWEEN AJO IMPROVEMENT AND ARIZONA**  
21 **WATER.**

22 A. Ajo Improvement provides treated water to Arizona Water  
23 through one delivery point. Arizona Water owns, operates  
24 and maintains booster pumps, two storage tanks, a  
25 distribution system, and other plant facilities necessary to  
26 provide reliable water service to its nearly 700 customers

1 and performs meter reading, customer billing and other  
2 customer services for its customers.

3 Commission Decision No. 54369 issued February 14, 1985,  
4 established a wholesale tariff and hourly (16,000 gph) and  
5 daily delivery limitations (384,000 gallons) which govern  
6 the way Arizona Water operates its storage tank pumping  
7 operations. That tariff specifies that no more than half of  
8 the actual daily consumption shall be taken between 7:00 AM  
9 and 7:00 PM. The delivery limitations relate to quantities  
10 of water delivered, authorizations necessary to exceed  
11 specified deliveries of water (referred to in the Decision  
12 as "requested overdraft"), and charges for deliveries in  
13 excess of the maximum quantities specified when they are not  
14 expressly authorized by Ajo Improvement.

15 Arizona Water's two storage tanks are operated in a  
16 manner that reduces peak, daily and hourly demand on Ajo  
17 Improvement's system while still meeting the needs of  
18 Arizona Water's customers. As such, Arizona Water's demand  
19 characteristics are typically off-peak, significantly  
20 differentiating its usage from that of Ajo Improvement's  
21 other customers and thereby greatly easing the burden on Ajo  
22 Improvement's water system.

23 In addition, Arizona Water does not have a large  
24 seasonal usage variation. Arizona Water's Ajo Height's  
25 system customer count, remains relatively constant  
26 throughout the year without large numbers of seasonal



1 residents.

2 Q. UNDER WHAT TARIFF DOES AJO IMPROVEMENT CURRENTLY PROVIDE  
3 WATER SERVICE TO ARIZONA WATER?

4 A. Currently, Arizona Water is served under Ajo Improvement's  
5 General Water Service tariff approved in Decision No. 54709  
6 issued on October 14, 1985. However, as discussed above,  
7 Arizona Water is not treated as a general service customer,  
8 but must take delivery of water as a wholesale customer in  
9 accordance with a delivery schedule and limitations in the  
10 wholesale tariff.

11 Q. HAVE YOU REVIEWED AJO IMPROVEMENT'S AND THE ACC STAFF'S  
12 RESPECTIVE RATE DESIGN PROPOSALS FOR THE 4-INCH METER TARIFF  
13 FOR TREATED WATER?

14 A. Yes. Based upon my review, Ajo Improvement is proposing a  
15 monthly minimum charge of \$210 and a single commodity rate  
16 of \$3.14 per 1000 gallons ("M gallons") for all water sold.  
17 The ACC Staff is recommending an inverted tier rate  
18 structure "to encourage efficient water use". More  
19 specifically, for the 4-inch meter, Staff is recommending a  
20 monthly minimum charge of \$234 and a two-block commodity  
21 rate design, \$2.90 for the first 180 M gallons and \$3.47 for  
22 all deliveries in excess of 180 M gallons. Neither Ajo  
23 Improvement or the ACC Staff are proposing to include any  
24 gallons in the monthly minimum charge.

25 Q. HAS ARIZONA WATER ANALYZED THE EFFECTS OF AJO IMPROVEMENT'S  
26 AND THE ACC STAFF'S PROPOSED RATE DESIGN ON FUTURE COSTS OF

1           **WATER FOR ARIZONA WATER?**

2    A.    Yes, we have.    Ajo Improvement is requesting an overall  
3           increase in revenues of 17.32% and proposing to increase the  
4           4-inch meter tariff for treated water by 23.35%.    The ACC  
5           Staff, on the other hand, is recommending an overall  
6           increase in revenues of 10.73% (Schedule CSB-1) while  
7           recommending a 35.7% increase for the 4-inch meter tariff  
8           for treated water (Schedule 19, page 6 of 19).    The ACC  
9           Staff's proposed rate design has the effect of imposing a  
10          35.7% increase in the cost of water for Arizona Water's 658  
11          5/8-inch customers while comparable sized customers in Ajo  
12          Improvement's service territory may actually see reductions  
13          in their rates based on the testimony of ACC Staff's  
14          witness, Ms. Crystal S. Brown.    Neither Ajo Improvement nor  
15          the ACC Staff have recommended a rate design that recognizes  
16          the service limitations under which Arizona Water receives  
17          water or excluded any of the costs that are not attributable  
18          to Arizona Water's service.

19    **Q.    IS THERE A FLAW INHERENT IN THE RATE DESIGN PROPOSED BY THE**  
20           **ACC STAFF?**

21    A.    Yes, there is.    The ACC Staff's witness recommends an  
22           inverted tier rate structure "to encourage efficient water  
23           use".    Because Ms. Brown's recommended rate design does not  
24           result in an increased bill for the 5/8-inch customer until  
25           consumption exceeds 6000 gallons, the intended result cannot  
26           be achieved because the average usage in the 5/8-inch

1 classification is 5700 gallons. Although there is a price  
2 signal at higher volumes under the ACC Staff's  
3 recommendation, a more appropriate rate design to encourage  
4 efficient water use would not place the entire burden of a  
5 recommended rate increase on the largest users. Staff is  
6 proposing an increase in gross revenue of \$68,833 (CSB-1,  
7 line 8), \$57,998 (84.26%) of this increase would be borne by  
8 Arizona Water as shown on Exhibit SLH-1.

9 **Q. AS A WHOLESALE CUSTOMER OF AJO IMPROVEMENT, PLEASE DESCRIBE**  
10 **ARIZONA WATER'S CUSTOMER MIX.**

11 A. Of Arizona Water's 689 customers, over 95%, or 658  
12 customers, are served through 5/8-inch meters and use 75.5%  
13 of the water. 29 customers are served through 1-inch meters  
14 and use 19.6% of the water, while 2 customers are served  
15 through 2-inch meters and use less than 2% of the water.  
16 The average monthly use by 5/8-inch customers is 5323  
17 gallons. Even so, most of the water Ajo Improvement  
18 delivers to Arizona Water would be billed at the above-6000  
19 gallon rate.

20 **Q. DOES AJO IMPROVEMENT PROVIDE ANY DISTRIBUTION SERVICES OR**  
21 **CUSTOMER-RELATED SERVICES FOR ARIZONA WATER'S CUSTOMERS?**

22 A. Ajo Improvement does not provide any distribution services  
23 or other customer-related services to Arizona Water's  
24 customers.

25 **Q. IS ARIZONA WATER THE ONLY CUSTOMER RECEIVING TREATED WATER**  
26 **SERVICE FROM AJO IMPROVEMENT USING THE 4-INCH METER?**

1 A. Yes. Based upon discussions with Ajo Improvement's witness,  
2 Mr. Dan Neidlinger, as well as the statistics included in  
3 their treated water bill count, Arizona Water is the only  
4 customer receiving treated water service from Ajo  
5 Improvement utilizing a 4-inch meter.

6 **IV. PROPOSED RATE DESIGN**

7 **Q. WHAT RATES ARE YOU PROPOSING FOR THE 4-INCH METER CUSTOMER**  
8 **USING TREATED WATER?**

9 A. Based upon an analysis of Arizona Water's customer  
10 characteristics, time of day pumping limitations and the  
11 characteristics of the delivery system and Ajo Improvement's  
12 proposed revenue requirement of \$752,767, Arizona Water  
13 proposes that it be served under a separate Wholesale Rate  
14 tariff consisting of the rates set forth on Exhibit SLH-2  
15 for Ajo Improvement's 4-inch meter classification. Arizona  
16 Water proposes a monthly minimum rate of \$210 and a  
17 commodity rate of \$2.67 per 1000 gallons.

18 **Q. PLEASE EXPLAIN THE RATIONALE SUPPORTING ARIZONA WATER'S**  
19 **RECOMMENDED RATE DESIGN PROPOSAL.**

20 A. Arizona Water purchases treated water from Ajo Improvement  
21 for resale purposes only. Arizona Water's customer base  
22 consists primarily of 5/8-inch meter customers with a small  
23 number of 1-inch and 2-inch meters. Ajo Improvement does not  
24 provide meter reading, billing or other customer-related  
25 services or any distribution-related services to Arizona  
26 Water's customers. Moreover, Arizona Water operates within

1 fixed hourly and daily pumping limits on a year-round basis.  
2 To reduce the potential cross-subsidy between Arizona  
3 Water's customers and Ajo Improvement's customers, a  
4 wholesale rate based on only the costs of serving Arizona  
5 Water should be developed to recover those costs. A rate  
6 design that recognizes the wholesale nature of the service  
7 provided by Ajo Improvement to Arizona Water is necessary to  
8 avoid the potential cross-subsidy.

9 **Q. WHAT METHODOLOGY HAS BEEN USED BY ARIZONA WATER TO SEGREGATE**  
10 **THE DISTRIBUTION CHARGES AND CUSTOMER SERVICE CHARGES FROM**  
11 **THE COST OF SERVICE APPLICABLE TO ARIZONA WATER?**

12 A. Generally, a cost of service study is utilized to segregate  
13 the cost to serve specific classes of customers. Absent the  
14 availability of a cost of service study, another method that  
15 identifies the specific costs incurred to provide treated  
16 water to Arizona Water can be used. I have proposed a rate  
17 design that recovers the variable cost of the treated water  
18 provided to Arizona Water and a fixed monthly meter charge  
19 to contribute to Ajo Improvement's fixed costs.

20 **Q. PLEASE DESCRIBE THE BASIS OF ARIZONA WATER'S RATE DESIGN**  
21 **PROPOSAL.**

22 A. Ajo Improvement purchases raw water directly from Phelps  
23 Dodge. The raw water is treated before it is served to Ajo  
24 Improvement's customers. Ajo Improvement has quantified the  
25 cost incurred for treated water at \$2.67 per 1000 gallons.  
26 See Ajo Improvement workpapers 000015 and 000016 attached as

1 Exhibit SLH-3. Arizona Water, therefore, is proposing a  
2 commodity rate of \$2.67 per 1000 gallons for the 4-inch  
3 wholesale rate in this proceeding. In addition, Ajo  
4 Improvement is proposing a monthly minimum charge of \$210  
5 for the 4-inch meter classification. Arizona Water  
6 recognizes that there are some fixed costs associated with  
7 providing wholesale water service and Arizona Water does not  
8 oppose the monthly minimum charge proposed by Ajo  
9 Improvement to cover these costs and the monthly billing  
10 charge. The revenue that results from Arizona Water's  
11 proposed rate design as shown in Exhibit SLH-1 is  
12 \$171,394.83.

13 Q. DOES THAT COMPLETE YOUR TESTIMONY IN THIS MATTER?

14 A. Yes, it does.

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# Exhibit SLH-1

## ARIZONA WATER COMPANY Ajo Improvement Company-Water Rate Increase Effect of Proposed Increase on Arizona Water

Line	Description	Water Usage (M Gal)	AIC's		Staff's		Arizona Water's	
			Present Rates	Proposed Rates	Increase	Proposed Rates	Proposed Rates	Increase
4" METERS:								
1	Monthly Service Charge		\$ 200.00	\$ 210.00	\$ 10.00	\$ 234.00	\$ 210.00	\$ 10.00
2	Commodity Rate per 1000 Gallons (1st Block)	180000	\$ 2.54	\$ 3.14	\$ 0.60	\$ 2.90	\$ 2.67	\$ 0.13
3	Commodity Rate per 1000 Gallons (2nd Block)	>180000	\$ 2.54	\$ 3.14	\$ 0.60	\$ 3.47	\$ 2.67	\$ 0.13
4	Arizona Water's 2002 Consumption	63,249	\$ 163,052.46	\$ 201,121.86	\$ 38,069.40	\$ 221,050.83	\$ 171,394.83	\$ 8,342.37
5 Detail of Effect of Proposed Increase on Arizona Water's 2002 Consumption:								
6	12-27-01 to 1-30-02	4,667	\$ 12,054.18	\$ 14,864.38	\$ 2,810.20	\$ 16,325.89	\$ 12,670.89	\$ 616.71
7	1-30-02 to 2-27-02	4,142	\$ 10,720.68	\$ 13,215.88	\$ 2,495.20	\$ 14,504.14	\$ 11,269.14	\$ 548.46
8	2-27-02 to 3-26-02	4,435	\$ 11,464.90	\$ 14,135.90	\$ 2,671.00	\$ 15,520.85	\$ 12,051.45	\$ 586.55
9	3-26-02 to 4-26-02	5,234	\$ 13,494.36	\$ 16,644.76	\$ 3,150.40	\$ 18,293.38	\$ 14,184.78	\$ 690.42
10	4-26-02 to 5-30-02	5,866	\$ 15,099.64	\$ 18,629.24	\$ 3,529.60	\$ 20,486.42	\$ 15,872.22	\$ 772.58
11	5-30-02 to 6-27-02	6,169	\$ 15,869.26	\$ 19,580.66	\$ 3,711.40	\$ 21,537.83	\$ 16,681.23	\$ 811.97
12	6-27-02 to 7-30-02	7,507	\$ 19,267.78	\$ 23,781.98	\$ 4,514.20	\$ 26,180.69	\$ 20,253.69	\$ 985.91
13	7-30-02 to 8-29-02	5,924	\$ 15,246.96	\$ 18,811.36	\$ 3,564.40	\$ 20,687.68	\$ 16,027.08	\$ 780.12
14	8-29-02 to 9-27-02	5,951	\$ 15,315.54	\$ 18,896.14	\$ 3,580.60	\$ 20,781.37	\$ 16,099.17	\$ 783.63
15	9-27-02 to 10-28-02	5,287	\$ 13,628.98	\$ 16,811.18	\$ 3,182.20	\$ 18,477.29	\$ 14,326.29	\$ 697.31
16	10-28-02 to 11-26-02	4,104	\$ 10,624.16	\$ 13,096.56	\$ 2,472.40	\$ 14,372.28	\$ 11,167.68	\$ 543.52
17	11-26-02 to 12-30-02	3,963	\$ 10,266.02	\$ 12,653.82	\$ 2,387.80	\$ 13,883.01	\$ 10,791.21	\$ 525.19
18	Totals	63,249	\$ 163,052.46	\$ 201,121.86	\$ 38,069.40	\$ 221,050.83	\$ 171,394.83	\$ 8,342.37
19	Proposed Gross Revenue Increase			\$ 111,125		\$ 68,833		111,125
20	Percentage of Proposed Increase Allocated to AWC			34.26%		84.26%		7.51%

Exhibit SLH-2

ARIZONA WATER COMPANY  
Ajo Improvement Company-Water Rate Increase  
Wholesale Rate Design - 4" Meter Size

Line	Description	Blocks	Present	-----Proposed-----			Arizona Water Proposed Increase to Present Rates
				Ajo Improvement	Staff	Arizona Water	
1	Monthly Service Charge		\$ 200.00	\$ 210.00	\$ 234.00	\$ 210.00	5.00%
2	Commodity Rate per 1000 Gallons	0 to 180,000	\$ 2.54	\$ 3.14	\$ 2.90	\$ 2.67	5.12%
3	Commodity Rate per 1000 Gallons	Over 180,000	\$ 2.54	\$ 3.14	\$ 3.47	\$ 2.67	5.12%



AJO IMPROVEMENT COMPANY  
TEST YEAR ENDED 12-31-02

Exhibit SLH-3  
Page 1 of 2

WATER DEPARTMENT  
COST OF TREATED  
AND UNTREATED WATER

DESCRIPTION	TOTAL	TREATED	UNTREAT.
Water Sales:			
Gallons Sold	206,024,846	162,358,586	43,666,260
Percent	100.00%	78.81%	21.19%
Purchased Water Cost:			
Raw Water @ \$1.08	\$232,392	\$183,137	\$49,255
PD Adder - 10%	23,239	18,314	4,925
Total Cost - Raw Water	\$255,631	\$201,451	\$54,180
Treatment Costs	266,682	266,682	
PD Adder - 10%	26,669	26,669	
Total Treatment Costs	\$293,351	\$293,351	\$0
Total Purchased Water Costs	\$548,982	\$494,802	\$54,180
Pro Forma Adjustments:			
Raw Water	(\$21,136)	(\$16,656)	(\$4,480)
PD Adder - 10%	(49,908)	(44,983)	(4,925)
Total Pro Forma Adjustments	(\$71,044)	(\$61,639)	(\$9,405)
Adjusted Purchased Water Cost	\$477,938	\$433,163	\$44,775
Cost Per 1,000 Gallons Sold	\$2.32	\$2.67	\$1.03

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AJO IM. JUVEMENT COMPANY  
TEST YEAR ENDED 12-31-02

WATER DEPARTMENT

PURCHASED WATER  
WATER TREATMENT CHGS.

DESCRIPTION	TOTAL 2002	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
Salaries/Exempt - Operating	\$94,484	\$9,055	\$6,936	\$8,146	\$8,552	\$9,648	\$5,842	\$4,867	\$5,673	\$6,534	\$8,105	\$11,974	\$9,152
Insurance/Flex - Hourly	666											666	
Reagents - Acid	218					112				106			
Water Treatment Chemicals	38,101	1,264	1,309	9,038	17,487	905	1,047	1,448	1,221	678	1,221	1,827	656
Freight Allocation - Acid Sales	950					473					477		
Other Operating Supplies	5,267	249	203	388	14			162	627	695	1,342	377	1,210
Maintenance & Repair Parts	1,247									1,247			
Outside Services - Other (1)	82,220	11,473	4,222	4,895	5,301	6,389	5,855	12,288	5,767	8,455	5,503	4,660	7,412
Employee Travel	100								100				
Employee Meals	12								12				
Allocation of Power	14,865	1,173	763	1,395	1,079	1,070	1,243	1,188	956	1,098	761	1,049	3,090
Allocation of Steam (2)	44,182	16,052	12,770	15,360									
Allocation of Benefits	28,549	2,749	2,110	2,473	2,594	2,923	1,608	1,460	1,702	1,960	2,432	3,792	2,746
Adjust. For Expense Elements	(7,322)			(7,322)									
	(44,182)			(44,182)									
	7,332			7,332									
	44,182			44,182									
Allocation to Water Treat. (2)	188,210				21,311	23,207	22,999	30,192	23,996	22,015	18,151	13,214	13,125
Transfer to BS - CIP Project (3)	11,203	4,202	2,831	4,170									
Adjust. For Expense Elements	(11,203)			(11,203)									
	11,203			11,203									
Transfer to BS - Accts. Rec.(3)	38,705				5,634	4,473	3,859	5,161	4,005	4,279	3,799	3,756	3,739
Total	\$548,989	\$46,217	\$31,144	\$45,875	\$61,972	\$49,200	\$42,453	\$56,766	\$44,059	\$47,067	\$41,791	\$41,315	\$41,130

NOTES:

- (1) Charges From Maintenance Contracting Firm
- (2) Purchased Raw Water from PD @ \$1.08 per thousand gallons
- (3) PD Add-On (10%) to Direct Charges